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Publication Information

Jay E. Grenig, When Is an Order Compelling Arbitration Subject to Appellate Review Under the Federal Arbitration Act?, 2000-01 Term Preview U.S. Sup. Ct. Cas. 13 (2000). © 2000 American Bar Association. This information or any portion thereof may not be copied or disseminated in any form or by any means or downloaded or stored in an electronic database or retrieval system without the express written consent of the American Bar Association.

Repository Citation

Grenig, Jay E., "When Is an Order Compelling Arbitration Subject to Appellate Review Under the Federal Arbitration Act?" (2000). *Faculty Publications*. Paper 384.

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When Is an Order Compelling Arbitration Subject to Appellate Review Under the Federal Arbitration Act?

by Jay E. Grenig

PREVIEW of United States Supreme Court Cases, pages 13–17. © 2000 American Bar Association.

Case at a Glance

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ISSUES

Did the Eleventh Circuit properly hold that a district court's order compelling arbitration and dismissing with prejudice the plaintiffs' individual and class claims constituted a "final decision" that was subject to immediate review under the Federal Arbitration Act?

Did the Eleventh Circuit properly hold that an arbitration clause was unenforceable because it was silent on the issue of costs and fees that the plaintiff might be required to bear in order to vindicate her statutory rights, and because it did not give the plaintiff the opportunity to use all the class action procedures available under the Truth in Lending Act?

FACTS

Larketta Randolph purchased a mobile home in 1994 from Better Cents Home Builders Inc., in Opelika, Ala. She financed her pur-

chase through Green Tree Financial Corp.—Alabama, a wholly owned subsidiary of Green Tree Financial Corporation (now known as Conseco Finance Corp.). According to Randolph, Green Tree required her to obtain "vendor's single interest" insurance, which protects a vendor or lienholder against the costs of repossession in the event of default. Green Tree did not mention this requirement in its Truth in Lending Act disclosure.

Randolph's installment contract with Better Cents named Green Tree as the assignee. The contract contained an arbitration agreement, providing, in part, as follows:

ARBITRATION; All disputes, claims or controversies arising from or relating to this Contract or the relations which result from this Contract, or the validity of this Contract, shall be resolved by binding arbitration by one arbitrator

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GREEN TREE FINANCIAL
CORPORATION—ALABAMA ET AL.
V. RANDOLPH
DOCKET NO. 99-1235

ARGUMENT DATE:
OCTOBER 3, 2000
FROM: THE ELEVENTH CIRCUIT

In this case, the Supreme Court is asked to decide whether an order compelling arbitration and dismissing a lawsuit's underlying claims is a "final decision" subject to immediate appellate review under the Federal Arbitration Act. It also must decide whether an arbitration provision that is "silent" on the issue of costs and fees should be unenforceable under the Act. The Eleventh Circuit answered "yes" to both questions, but the Supreme Court has agreed to review those rulings.

selected by Assignee with consent of Buyer(s). This arbitration Contract is made pursuant to a transaction in interstate commerce, and shall be governed by the Federal Arbitration Act at 9 U.S.C. Section 1. Judgment upon the award rendered may be entered in any court having jurisdiction. The parties agree and understand that they choose arbitration instead of litigation to resolve disputes. The parties understand that they have a right or opportunity to resolve their disputes through arbitration, except as provided herein. THE PARTIES VOLUNTARILY AND KNOWINGLY WAIVE ANY RIGHT THEY HAVE TO A JURY TRIAL EITHER PURSUANT TO ARBITRATION UNDER THIS CLAUSE OR PURSUANT TO A COURT ACTION BY ASSIGNEE (AS PROVIDED HEREIN). The parties agree and understand that all disputes arising under case law, statutory law, and all other laws including, but not limited to binding arbitration in accord with this Contract. The parties agree and understand that the arbitrator shall have all powers provided by the law and the Contract ... [including] money damages, declaratory relief, and injunctive relief. Notwithstanding anything hereunto the contrary, Assignee retains an option to use judicial or nonjudicial relief to enforce a security agreement related to the Manufactured Home or to foreclose on the Manufactured Home. ... The initiation and maintenance of an action for judicial relief in a court [on the foregoing terms] shall not constitute a waiver of the right of any party to compel arbitration regarding any other dispute or remedy subject to arbitration in this Contract, including the filing of a counterclaim in a suit brought by the Assignee pursuant to this provision.

In January 1996, Randolph brought suit in federal court alleging that

Green Tree had violated the Truth in Lending Act (15 U.S.C. § 1601 et seq.) by failing to include the requirement of vendor's single interest insurance in its Truth in Lending Act disclosure and had violated the Equal Credit Act (15 U.S.C. §§ 1691-1691(f)) by requiring arbitration of all claims. Randolph sought certification of a class of individuals who had entered into similar agreements with Green Tree. In response to the suit, Green Tree moved to compel Randolph to arbitrate her complaint pursuant to the arbitration agreement. Green Tree also moved to stay the action pending arbitration or, in the alternative, to dismiss it.

The district court granted the motion to compel arbitration and declined to certify a class. *Randolph v. Green Tree Financial Corp.*, 991 F.Supp. 1410 (M.D.Ala. 1997). Concluding that all the issues raised in Randolph's complaint must be submitted to arbitration, the court dismissed her claims with prejudice. Randolph then sought review in the Eleventh Circuit.

The Eleventh Circuit reversed the district court and held that if an arbitration issue arises as part of a broader action involving other issues, and if the district court effectively disposes of all other issues by issuing an order compelling arbitration and dismissing the remaining claims with prejudice, the order is an appealable "final decision." Examining the language of the Federal Arbitration Act, the Eleventh Circuit determined that the phrase "final decision" was a term of art that was of long standing when Congress enacted Section 16(a)(3) of the Federal Arbitration Act. The court reasoned that a dismissal with prejudice clearly is a decision that ends the litigation on the merits and leaves nothing for

the court to do but execute on the judgment.

The Eleventh Circuit reasoned that the arbitration clause signed by Randolph in this case was unenforceable because it failed to provide minimum guarantees required to ensure that she could vindicate her statutory rights under the Truth in Lending Act. The Eleventh Circuit stated that when an arbitration clause has provisions defeating the remedial purpose of a statute, the clause is not enforceable.

According to the court, the arbitration clause in this case raised serious concerns with respect to filing fees, arbitrators' costs, and other arbitration costs that might curtail Randolph's access to the arbitral forum. The court explained that the clause said nothing about the payment of filing fees or the apportionment of costs of arbitration, and that it did not provide for a waiver in cases of financial hardship. The court also noted that the clause did not say whether consumers, if they prevail, will nonetheless be saddled with fees and costs in excess of any award. Additionally, the court found that the clause did not say whether the rules of the American Arbitration Association, which provide guidelines concerning filing fees and arbitration costs, apply to the proceeding, whether some other set of rules applied, or whether the parties must negotiate their own set of rules. The United States Supreme Court agreed to review the Eleventh Circuit's decision. 120 S.Ct. 1552 (2000).

CASE ANALYSIS

Section 16 of the Federal Arbitration Act sets forth special rules governing appeals from a district court's arbitration order. Under Section 16, an appeal may be taken

from an order that somehow prevents arbitration from going forward. An appeal may also be taken from “a final decision with respect to an arbitration that is subject to this title.” 9 U.S.C. § 16(a)(3). Appeals may not be taken, however, from “interlocutory orders” that in one way or another allow the arbitration to proceed. *Napleton v. General Motors Corp.*, 138 F.3d 1209, 1216 (7th Cir.1998).

The question presented in this case is whether the district court’s order compelling arbitration and dismissing Randolph’s claims with prejudice was a “final decision with respect to an arbitration.” In considering this question, a number of circuits have distinguished between “embedded” and “independent” proceedings. An “embedded” proceeding is one in which the arbitration issue arises as part of a broader action dealing with other issues. For example, in this case, Randolph alleged a substantive violation of the Truth in Lending Act in addition to raising the arbitrability question. In an “independent” proceeding, on the other hand, the motion to compel arbitration is the only issue before the court.

Green Tree argues that an order compelling arbitration and dismissing an “embedded” proceeding is not a “final decision” under the Federal Arbitration Act. According to Green Tree, settled statutory construction principles govern the scope of appellate jurisdiction under the Act, and they preclude an appeal in this case. Green Tree asserts that the Purpose of the Federal Arbitration Act and the structure of Section 16 confirm that an order compelling arbitration in an “embedded” proceeding is not a “final decision” under Section 16.

Disagreeing with Green Tree, Randolph argues that the order dis-

missing the action with prejudice was a “final decision” under the Federal Arbitration Act. She asserts that the plain language of Section 16(a)(3) and prior case law indicate that a dismissal with prejudice is a final decision.

As to the enforceability of the arbitration clause, it is Green Tree’s position that the Federal Arbitration Act reflects a strict presumption in favor of arbitration of federal statutory claims. It argues that the arbitration agreement is enforceable to resolve Randolph’s claims under the Truth in Lending Act and that Congress did not intend to preclude individual agreements to arbitrate Truth in Lending Act claims.

Randolph contends that the arbitration agreement was unenforceable because it compromised her ability to enforce her statutory rights under the Truth in Lending Act. According to Randolph, the agreement was unenforceable because it failed to ensure that the costs she would bear in arbitration were no greater than those that she would have incurred in court. She also argues that the arbitration agreement is unenforceable because it prevented her and putative class members from proceeding on a class action basis, thereby effectively denying a remedy to the entire class.

SIGNIFICANCE

The Supreme Court is faced with a split in the circuits on the question of whether a district court’s order compelling arbitration in an embedded proceeding is an appealable “final decision” when it dismisses the remaining claims. Eight circuits (the First, Second, Third, Fourth, Fifth, Seventh, Eighth, and Ninth) have held that orders compelling arbitration arising in embedded pro-

ceedings must be treated as “interlocutory” and not final decisions under Section 16(a)(3).

The Ninth Circuit explained that if the substantive suit is pending, a district court’s decision to compel arbitration of some or all of the claims before it is not considered to be final and therefore is not reviewable. In most embedded proceedings, orders compelling arbitration are treated as interlocutory because, after the arbitrability issue has been decided, other issues remain in the case for the district court to resolve. Accordingly, an order directing the parties to proceed to arbitration could not be considered a “final decision” under Section 16(a)(3).

Where the district court’s dismissal of the action leaves no additional issues for it to resolve, the First, Fifth, Seventh, Eighth, and Ninth Circuits have held that a dismissal of an embedded proceeding without prejudice is not appealable. Like the Eleventh Circuit, the Sixth and Tenth Circuits have also treated dismissal of a plaintiff’s remaining claims with prejudice as an appealable final decision.

In *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S. 20 (1991), the Supreme Court held that, as a general rule, statutory claims are fully subject to binding arbitration. The Court explained that “[b]y agreeing to arbitrate a statutory claim, a party does not forgo the substantive rights afforded by the statute; it only submits to their resolution in an arbitral, rather than a judicial, forum.” So long as the prospective litigant may vindicate his or her statutory cause of action in the arbitral forum effectively, the Court stressed that the statute will continue to serve both its remedial and deterrent functions. *See also*

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Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614 (1985).

If the terms of an arbitration agreement actually prevent an individual from effectively vindicating his or her statutory rights, the clause is not enforceable. *Shankle v. B-G Maintenance Management of Colorado, Inc.*, 163 F.3d 1230 (1999). Because the beneficiaries of public statutes are entitled to the rights and protections provided by the law, an arbitration agreement covering statutory rights is not entitled to enforcement regardless of what rights it waives or what burdens it imposes. *Cole v. Burns Int'l Security Services, Inc.*, 105 F.3d 1465 (D.C.Cir. 1997).

In *Paladino v. Avnet Computer Technologies, Inc.*, 134 F.3d 1054 (11th Cir. 1998), the Eleventh Circuit held that forcing the plaintiff to bear the brunt of "hefty" arbitration costs and "steep filing fees" constitutes a legitimate basis for concluding that an arbitration clause does not comport with statutory policy. See also *Cole v. Burns Int'l Security Services, Inc.*, 105 F.3d 1465 (D.C.Cir. 1997) (requiring an employer to bear the sole costs of an arbitrator's fees where the arbitration was imposed by the employer could preclude enforcement of an arbitration agreement).

On the other hand, in *Rosenberg v. Merrill Lynch, Pierce, Fenner & Smith*, 170 F.3d 1 (1st Cir. 1999), the court of appeals held that New York Stock Exchange arbitration procedures were enforceable to arbitrate an employment discrimi-

nation claim where the record suggested that most successful arbitral claimants were awarded fees and costs. And in *Doctor's Associates, Inc. v. Stuart*, 85 F.3d 975 (2d Cir. 1996), the Third Circuit enforced an arbitration agreement where the plaintiff's estimated total costs of arbitration were between \$28,000 and \$32,000 and the arbitration clause arose in the context of a commercial franchise agreement rather than in a small consumer transaction or employment agreement.

The cost of an arbitration proceeding may be substantial. See Edwards, "Where Are We Heading with Mandatory Arbitration of Statutory Claims in Employment?" 16 *Georgia State University Law Review* 293, 306 (1999). Edwards suggests that while "some courts still subscribe to the fond, but misguided view that employment arbitration is invariably quick and cheap," an average case may result in arbitrator fees ranging from \$3,750 to \$14,000.

According to the *Wall Street Journal*, arbitrators may charge up to \$600 per hour. An article in the *New York Law Journal* listed cases involving arbitration fees between \$24,000 and \$82,000. Brecher, "Putting the Reins on Employment Arbitration: Courts Safeguard Employee Rights," *N.Y.L.J.* (Aug. 24, 1999).

Some courts will not permit class actions to proceed through arbitration in the absence of an express provision for them. See, e.g., *Champ v. Siegal Trading Co.*, 55 F.3d 269 (7th Cir. 1995) (holding

that Section 4 of the Federal Arbitration Act requires that the agreement be enforced as drafted, precluding class actions absent an express provision for them).

Other courts have declined to enforce arbitration agreements that would have foreclosed the availability of class actions under the Truth in Lending Act and other consumer statutes. See, e.g., *Johnson v. Tele-Cash, Inc.*, 85 F.Supp.2d 264 (D.Del. 1999).

A similar case involving the Truth in Lending Act is presently pending before the U.S. Court of Appeals for the Third Circuit. In that case, the district court denied the defendants' motion to compel arbitration. *Johnson v. Tele-Cash, Inc.*, 82 F.Supp.3d 264 (D.Del. 1999). The district court held that there was an "inherent conflict" between the Truth in Lending Act's provision for class actions and arbitration.

This case provides the Court with an opportunity to clarify its holding in *Gilmer* that, as a general rule, statutory claims are fully subject to binding arbitration. In addition, the Court may provide guidance as to when a decision compelling arbitration may be appealed. Given the increase in agreements purporting to require arbitration of statutory claims, this decision will have a substantial impact on businesses as well as consumers and employees.

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**AMICUS BRIEFS (AS OF
SEPT. 1)**

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